3C. Strategic Principles	Agenda

We will enhance our Competitiveness with these five strategies:

I. Maximize Marlboro's share growth to grow our total share

II. Protect existing OPB share without interfering with Marlboro's growth

III. Protect PM's share of discount without interfering with Marlboro's growth

IV. Develop new products/product technologies that meet requirements of proposed resolution

V. Align the distribution systems' goal with ours

2073275710

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

This section looks at the alignment of distribution from three points of view:

- Our salesforce
- Retail trade
- Wholesale trade

2073275711

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Our salesforce is key to distribution and since 1992 we have made great strides in executing against our three core sales strategies.

1. Simplify Retail Execution
   - Developed "PM Express" POS delivery
   - Hired Third Party Installers
   - Placed more focus on selling/category management
   - Introduced a new National Promotion process
2. Optimize the Distribution System
   - Replaced "Retail Row" programs with "pay for performance" program
   - Gained access to "Distributor-to-Retailer" shipment data
   - Introduced a distributor assembly and delivery program (DAD)
3. Develop a People Advantage
   - Established new key performance measures
   - Set up Learning Centers for sales managers
   - Implemented Variable Pay to reward results
   - Assigned Top 50 accts to RVPs and SSDs

2073275712

Source: Trade Marketing

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

The number of Territory Sales Managers (TSMs) has remained fairly constant over the years while productivity has risen.

2073275713

Source: SPACE (run date: 1/26/98)

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

We have further actions planned.

Simplify Retail Execution

- Identify & eliminate non-value added activities
- Utilize technology in execution process
- Design measurable milestones
- Expand audit of retail promotions

Optimize the Distribution System

- Develop new sales and account management business models
- Establish greater data/order entry link with customers via Genesis

Expand our People Advantage

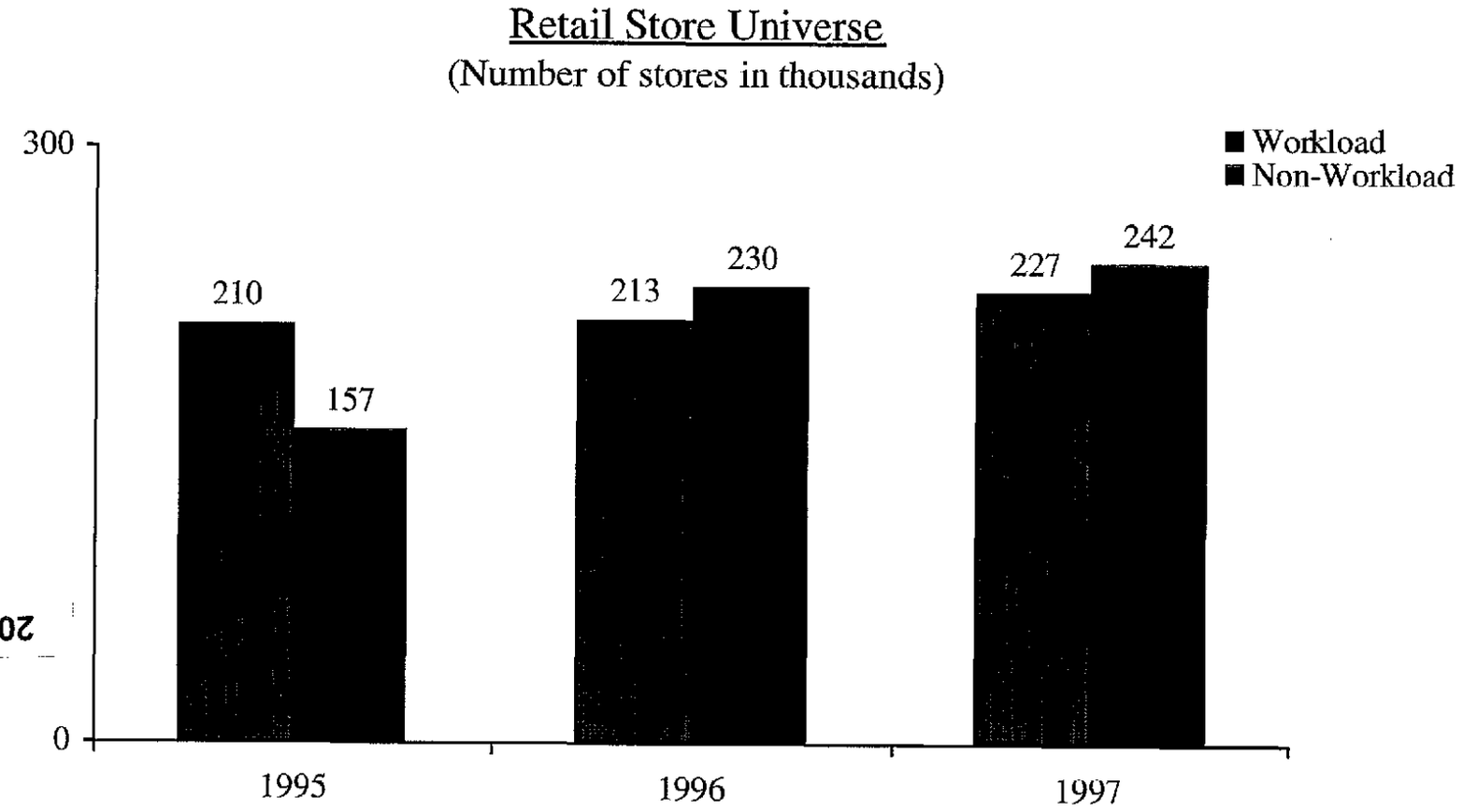
- Analyze optimal size and structure of sales force
- Improve FSF capabilities and performance metrics

2073275714

Source: Trade Marketing

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

The number of workload stores has increased by 6.5% to approximately 227,000 in 1997, while the number of non-workload stores has increased by 5.2%.



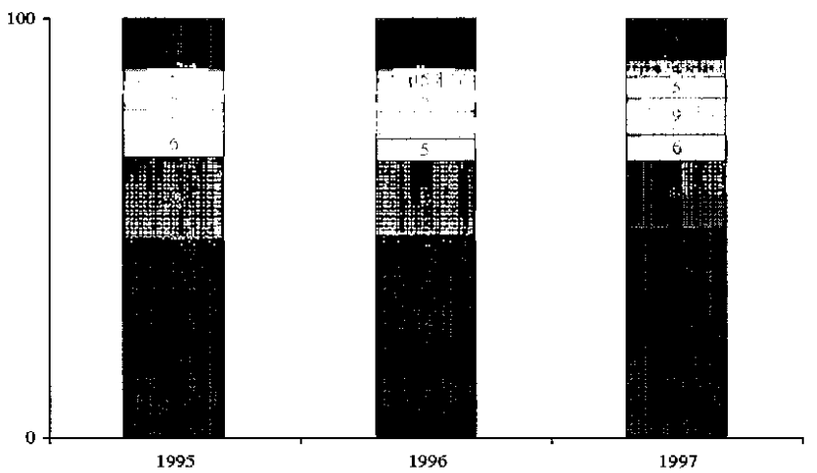
Source: Trade Marketing, SPACE (run date: 1/25/98), WM participants

2073275715

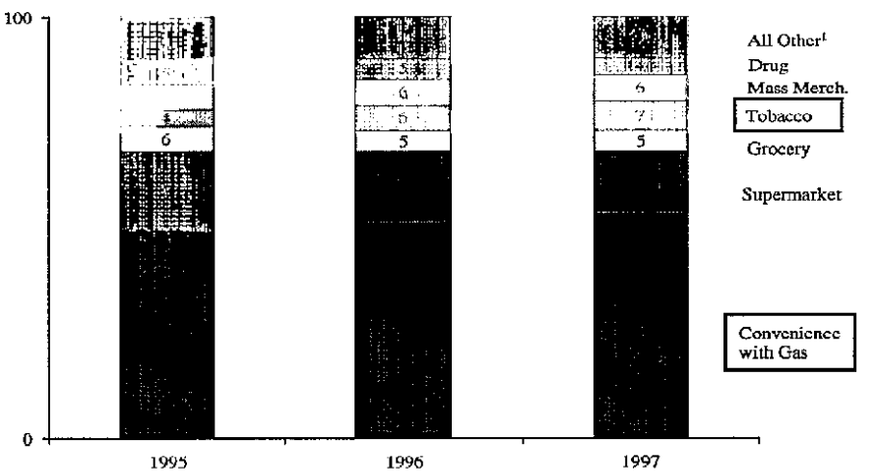
Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Convenience stores and tobacco stores both continue to grow primarily at the expense of supermarkets and drug stores.

In the industry as a whole...



...and for PM.



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[1] Includes Liquor, Native American, Wholesale Clubs, and Newstand.
Source: SFA

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Big Players are becoming bigger and PM continues to grow share amongst these strong players.

Top 10 Retail Chains per Trade Class

	% Total Industry Volume			Total PM Share		
	FY '96	YTD '97 (w/e 11/22/97)	Chg.	FY '96	YTD '97 (w/e 11/22/97)	Chg.
C-Store/Gas	16.39	17.72	1.33	52.89	54.04	1.15
Drug	65.49	71.72	6.23	50.39	51.01	0.62
Grocery	11.41	11.74	0.33	41.42	43.55	2.13
Mass Merch.	58.03	65.83	7.80	56.01	62.15	6.14
Supermarket	27.97	37.03	9.06	47.79	49.47	1.68

2073275717

Source: STARS store level (w/e 11/22/97)/MSI Department

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Distribution for the major PM brands has remained relatively constant from 1996 to 1997, with the exceptions of a slight gain for Basic and reductions for Cambridge and Private Label brands.

Selected PM Brand Distribution
(% Stores Selling)

	Total U.S. - AOC			Total U.S. - C-Stores		
	1996	1997	Chg.	1996	1997	Chg.
Marlboro	100	100	0	100	100	0
Basic	88	90	+2	91	92	+1
B & H	97	97	0	97	97	0
Merit	98	98	0	98	98	0
V. Slims	98	98	0	98	98	0
Parliament	55	55	0	49	50	+1
Cambridge	69	62	-7	67	60	-7
Private L.	17	15	-2	18	16	-2

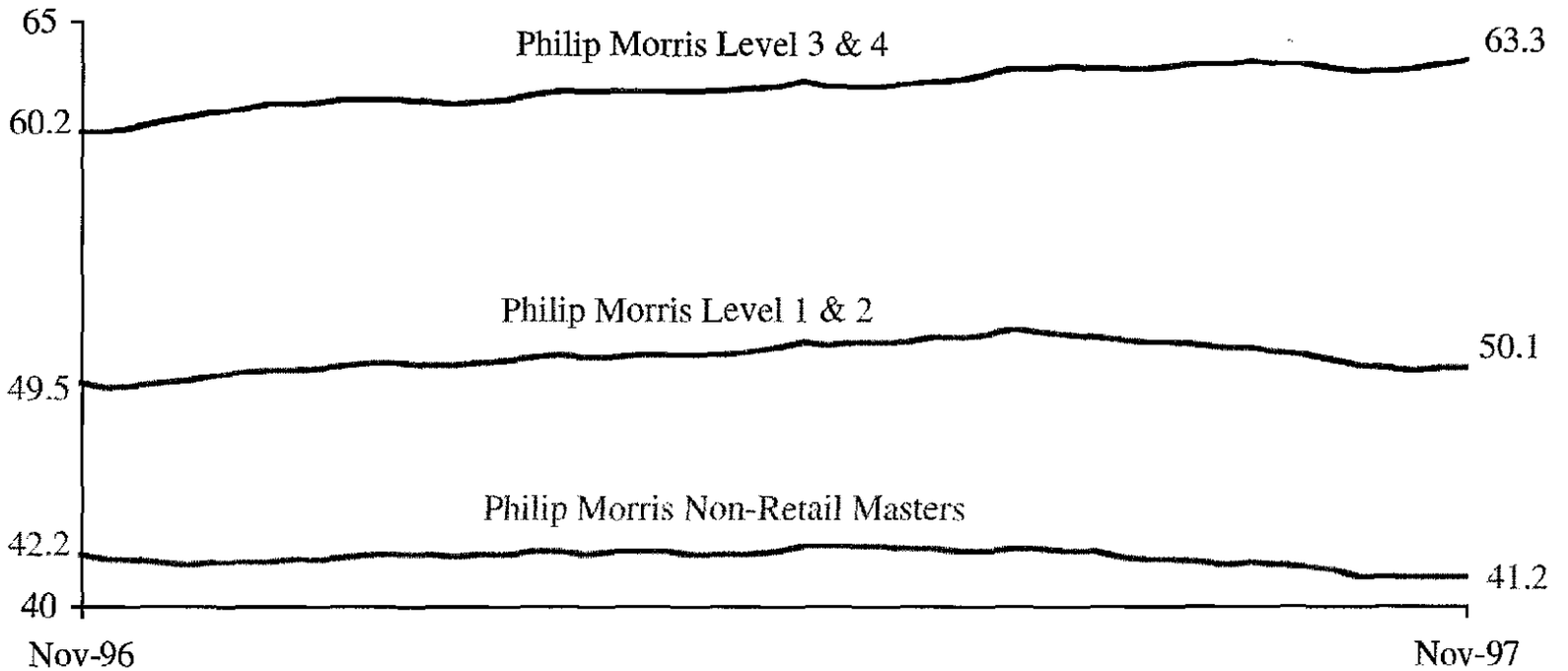
Source: Nielsen (run date: Jan. '97 & Jan. '98)

2073275718

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Measured by our share performance, which is positive, Retail Masters continues to be an effective tool to motivate the retailers.

Philip Morris
All Outlets Combined - Total U.S.
(13wm Share)



Source: STARS store level (11/22/97)
MS&I Dept.

2073275719

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Retail Masters continues to build share for the company in almost all trade classes with levels 3 and 4 all being positive.

Share Change Retail Masters
(% Nov 97 vs. Nov 96 YTD 13wm)

	Levels			
	1 & 2	3 & 4	1 - 4	Non-Retail Masters
C-Stores	0.2	1.5	0.7	0.6
Drug Stores	1.4	0.5	1.2	(0.6)
Supermarkets	0.8	2.0	1.6	(0.2)
Tobacco Stores	(0.4)	5.5	0.7	(3.4)
Mass Merch.	(0.1)	7.5	7.3	0.8
AOC	0.6	3.1	1.5	(1.0)

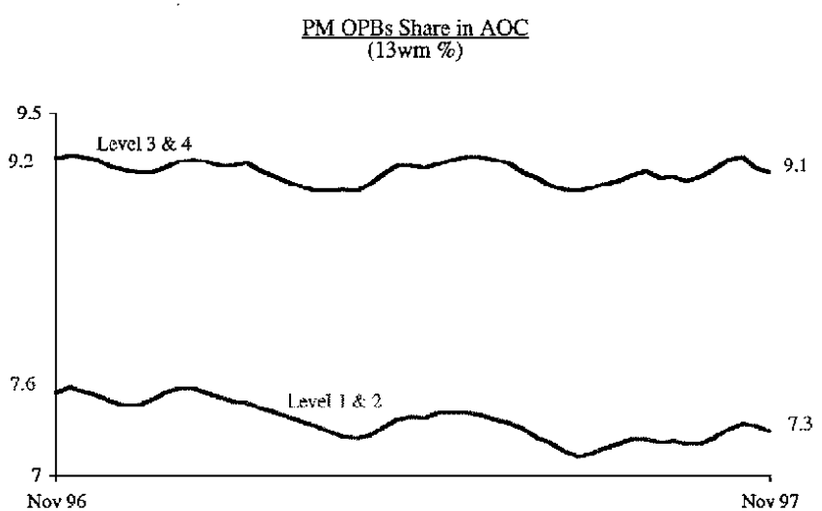
2073275720

Source: STARS store level (11/22/97)
MS&I

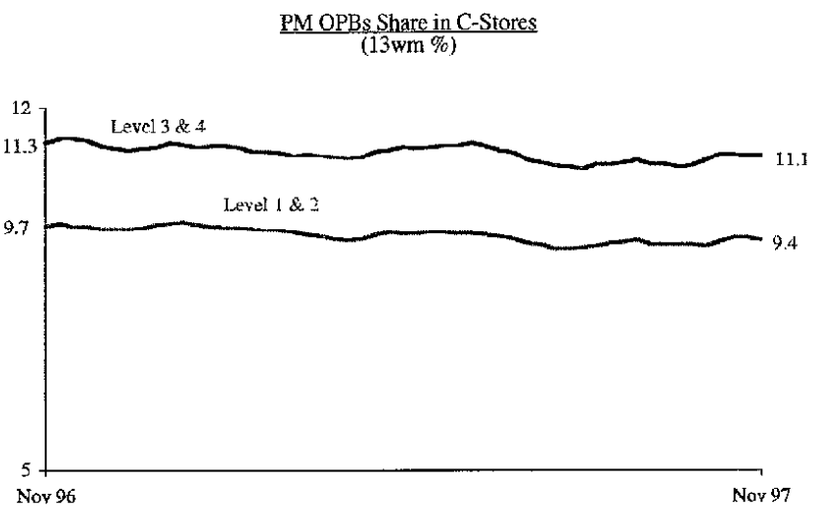
Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Opportunity #1: Our OPB's are underperforming in Retail Masters accounts.

This is true in AOC...



...and in C-Stores.



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Source: STARS store level (11/22/97)
MS&I

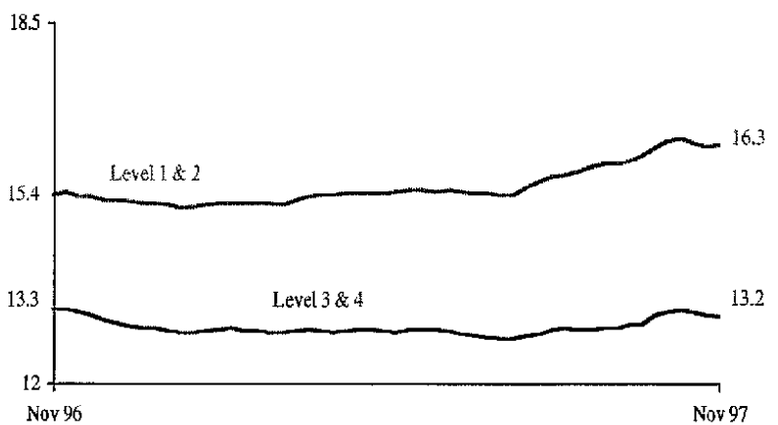
Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Core competitive premium brands (Winston, Camel, Newport) do well in Retail Masters Level 1 & 2 accounts where they are gaining share and are holding share in Levels 3 & 4.

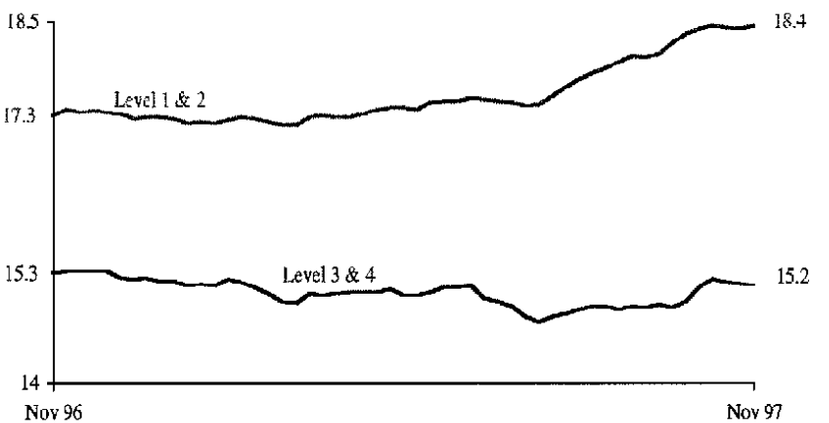
Their share is up 0.9 share points in AOC...

...and 1.1 share points in C-Stores

Core Competitive Premium Brands ' Share in AOC
(13wm Share)



Core Competitive Premium Brands' Share in C-Stores
(13wm Share)



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Source: STARS store level (11/22/97)
MS&I

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Opportunity #2: There is an opportunity for gaining share in non-Retail Masters outlets which represent 43% of our volume but 49% of industry volume.

	% PM Volume Contribution		% Industry Volume Contribution	
NRM (Workload)	30	43	49	35
Non-Workload	13			14
MLP1	5			5
MLP2	28			26
MLP3+	25			20

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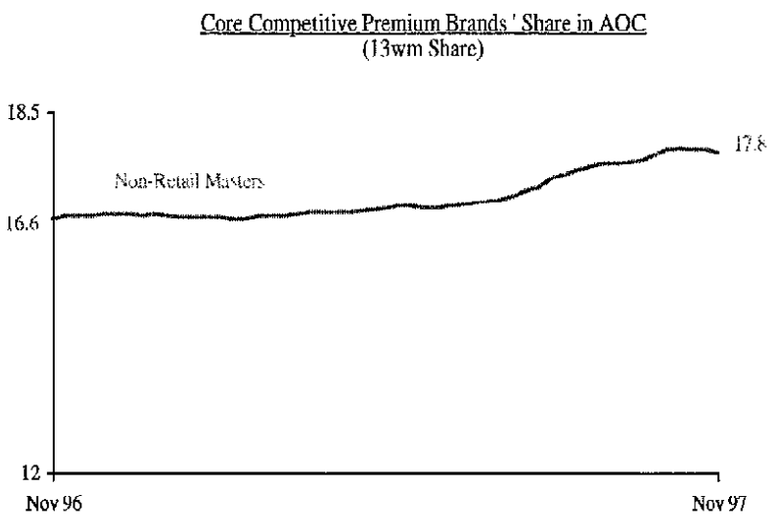
Source: STARS store level (11/22/97)

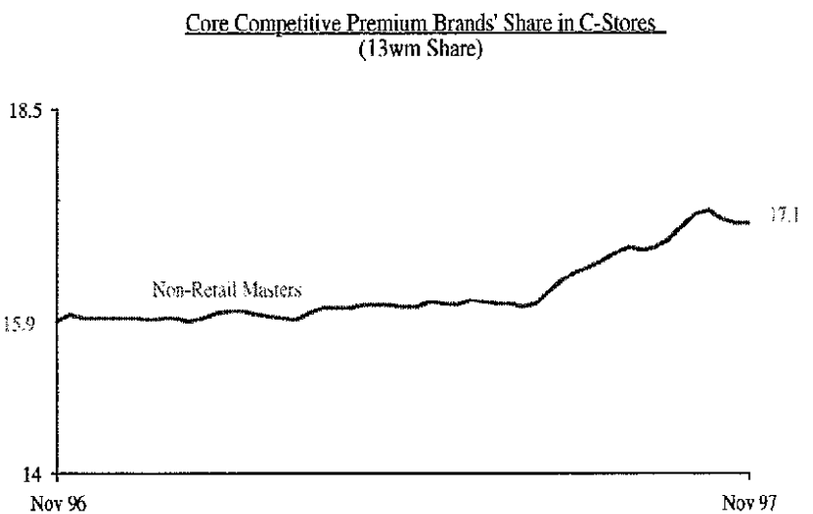
Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

The strength of core competitive premium brands (Winston, Camel, Newport) in non-Retail Masters accounts is evident.

Their share is up 1.2 share points in AOC...



...and 1.2 share points in C-Stores



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Source: STARS store level (11/22/97)
MS&I

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Opportunity #3: Distribution in Metro areas has been an issue which we are addressing.

Our YAS share in Metro areas was low, particularly vs. Newport...

YAS Share
(%)

	National		Region 1	
	U.S.	Metro	Reg.	Metro
Marlboro	61	50	51	37
Newport	15	30	30	48

...but our new Metro program is greatly broadening our reach.

Incremental Activities
New Metro Program

- 23 markets
- 20,000 workload stores
- 10,000 "Powerforce" stores[1]
- 500,000 POS pieces
- Six retail promotions in '98
- Examining OPB opportunities

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[1]Third party that provides supplemental coverage for stores with less than 20 cartons sold per week in 14 urban markets.
Source: CTS 12mm 6/97 (Urban Prizm Clusters/sample size of 233 age LA-24 smokers)
Marlboro Brand Group

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

We continue to work on a number of retail initiatives.

1998 Actions Underway

Motivate RM accounts to continue to focus on the cigarette category both SS and LNSS retail environment.

- Increase Flex Fund (additional 5¢/ctn.)
- Extend Marlboro price-off promotion periods
- Introduce new NSS contracts/merchandising rack systems
- Explore ways to improve OPBs performance in RM Level 1 & 2

Tap into potential of non-RM/ non-workload store universe.

- Expand Marlboro Metro Program
- Examine OPB opportunity

2073275726

Source: PM Business Planning and Trade Marketing

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

This section looks at the alignment of distribution from three points of view:

- Our salesforce
- Retail trade
- Wholesale trade

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Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

PM volume continues to grow for all direct accounts participating in Wholesale Masters.

Wholesale Masters Participation

	1995	1996	1997
% PM Volume	89.3	91.1	95.7
Direct Accounts (#)	906	1033	1040

2073275728

Source: MSA (run date: 1/26/98)
Trade Marketing

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

And in 1997 the top ten Direct Customers accounted for 40% of PM volume up from nearly 36% in 1996.

Wholesale Trade
Top Ten Direct Customers
(Avg. week sales in millions of units)

	1996		1997		
	Avg.Week Sales	% Volume Contrib. to PM	Avg.Week Sales	% Volume Contrib. to PM	pp Volume Contrib. to PM Change
Top 10	1,583	35.9	1,811	40.0	+4.1
Top 100	3,049	69.3	3,278	72.3	+3.0
Total PM	4,402	100.0	4,532	100.0	–

2073275729

McLane Company increased its percent volume contribution to PM by 4.0pp to 20.4% in 1997.

Source: Top Ten Customer Report (run date: 12/26/97)
PM-USA Mgt. Weekly Sales Top 300 (Dec '96 & Dec '97)
MS&I Department

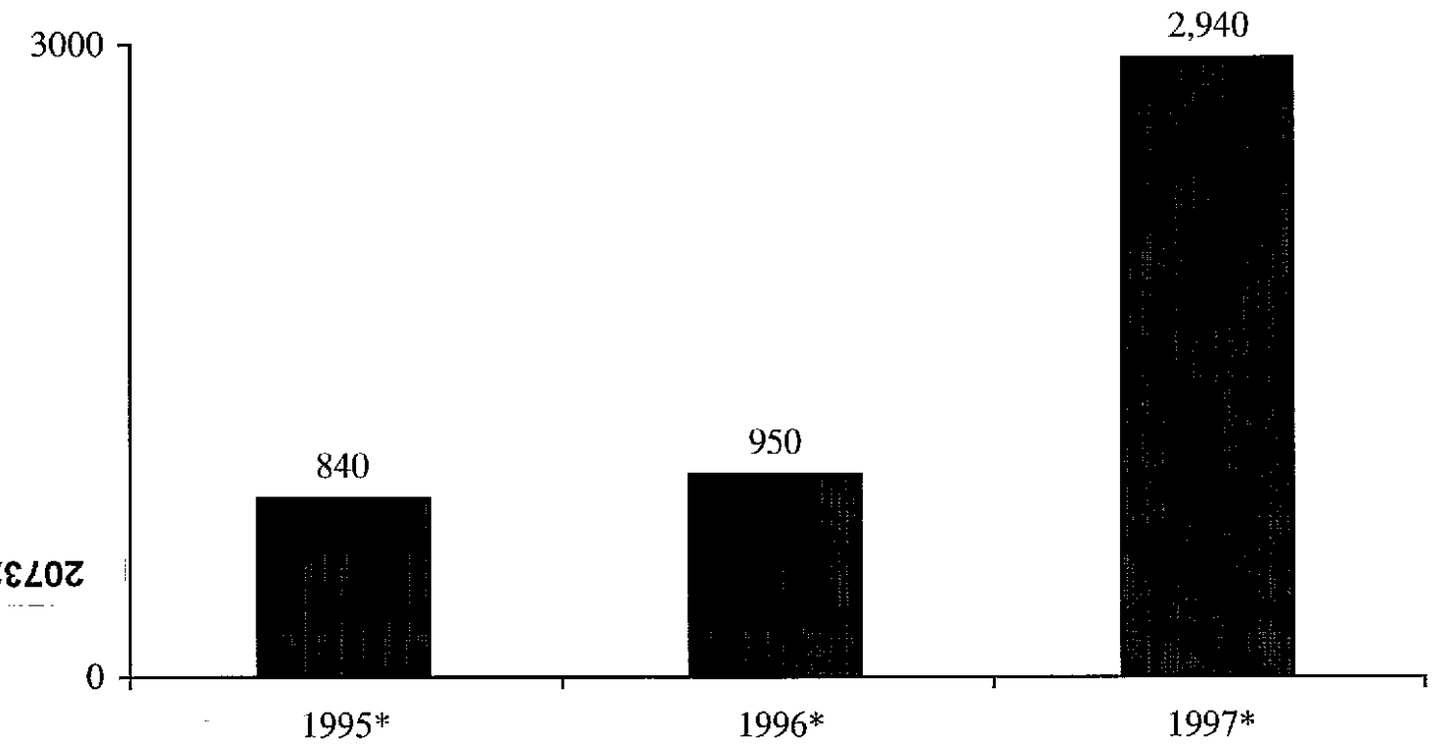
Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

3C. Strategic Principles	2. Competitiveness

V. Distribution	Wholesale trade

Wholesalers played a significantly greater role in the execution of PM promotion programs/events, distributing nearly 3 million kits in 1997 to participating retailers.

PM Express Kits Distributed to Wholesalers
(000s)



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* Madden fiscal years (Nov. - Oct.)
Source: PM Express, Jan. 1998

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Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

The 10% penalty provision under the Wholesale Masters program has improved the timeliness and accuracy of weekly retail shipment data.

Late data submissions have been reduced.

The accuracy of submitted retail promotion data has also improved.

Late Data Submissions

	4Q'96	4Q'97	% Chg.
#Accts.	423	93	(78)

Promotion Reports with Errors

	3Q'97	4Q'97	% Chg.
#Accts.	268	156	(42)

2073275731

Source: MSA, Trade Marketing Department

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

The Wholesale Masters program is working well for us but we are implementing some upgrades.

Expand distributor involvement.

- Reduce Business Acquisition Requirement from 20% to 15%.
- Reduce target cap from 61.9% to 58.9%.
- Increase maximum carton earnings by 1¢/carton to 23¢.

Enhance support of field sales force.

- Aggressively support and gain retail acceptance of new product introductions.
- Minimize out of stocks.
- Assemble retail promotions.
- Distribute PM Express kits.
- Support Metro store coverage.

Establish greater technological link with direct accounts

- Optimize use of electronic commerce to improve customer's sales forecasts and inventory management.
  - Pilot programs are underway with McLane and Food Lion.
- Explore a "PM Extranet" for communicating new products, pricing, and/or tele-selling.

2073275732

Source: PM Trade Marketing, Customer Service & Business Planning

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

3C. Strategic Principles	Agenda

We will manage the business according to these principles:

1. Price above settlement/proposed resolution costs and slightly in excess of inflation to provide modest margin enhancement.
2. Enhance ***Competitiveness***.
3. Reduce ***Costs*** in order to maintain our total cost per thousand assuming our volume declines.
4. Ensure we have the ***Capability*** to deliver the results we need to operate within the letter and spirit of the proposed resolution by attracting, hiring, and retaining a highly motivated, performance driven and proud workforce.
5. Ensure regulatory ***Compliance*** by designing and implementing a quality system that meets the business needs and helps offer society the opportunity to more positively view our company and our products.

2073275733

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

There has been a 15.9% reduction in the PM-USA workforce since 1992; with nearly 75% of the reduction consisting of hourly and part-time workers.

PM-USA Workforce Population
(Number of Employees)

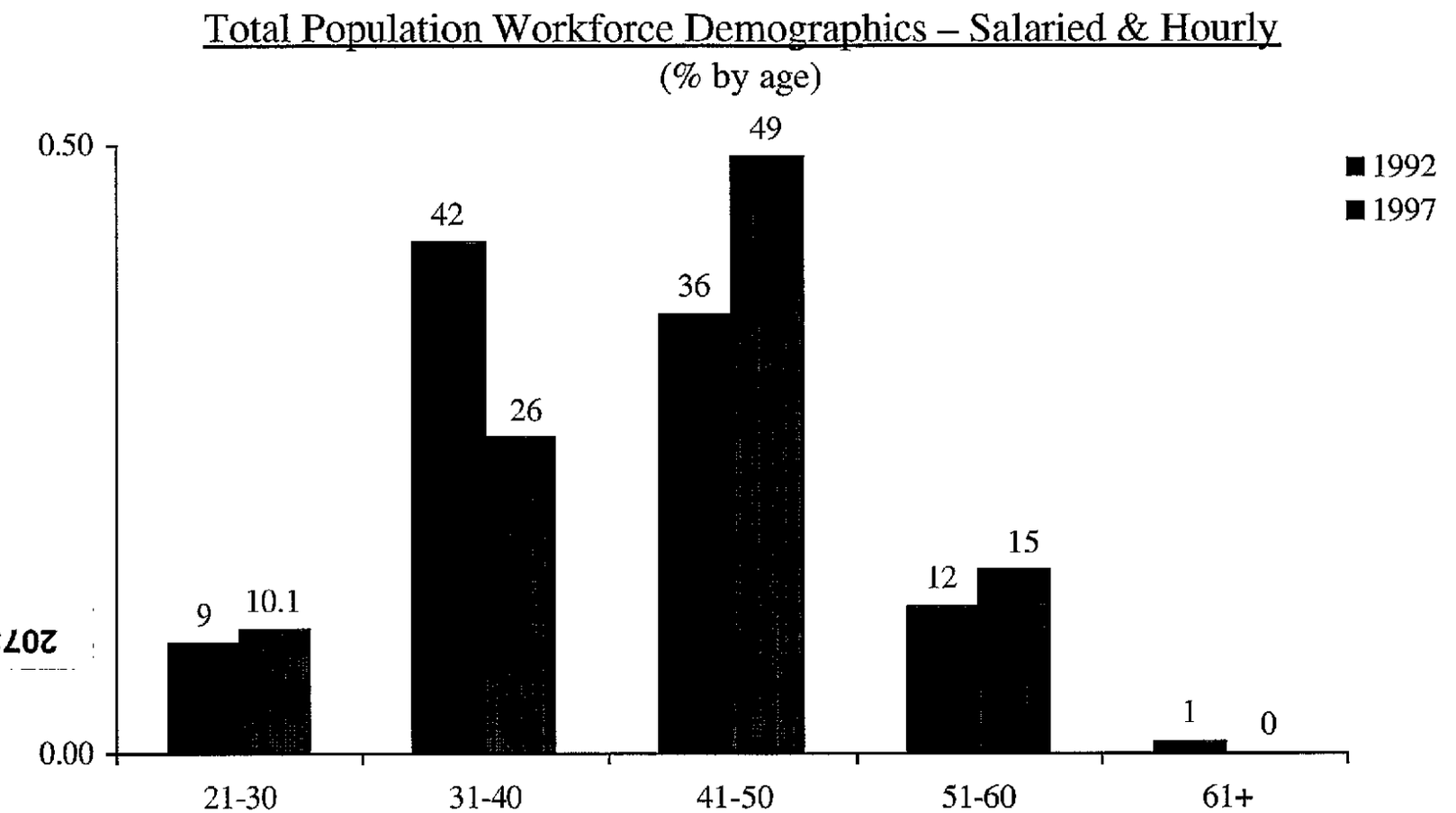
	1992	1997[1]	Change #	Change %
Total	19,404	16,322	-3,082	-15.9
Reg. Salaried	8,801	7,945	-856	-9.7
Exempt	7,061	6,557	-504	-7.1
Non-Exempt	1,740	1,388	-352	-20.2
Hourly	9,898	8,253	-1,645	-16.6
Part-time	636	22	-614	-96.5
Temporary[2]	69	102	+33	+47.8

2073275734

[1] Through 12/31/97
[2] College Interns (the majority employed by Sales and Manufacturing/R&D)
Source: Tesseract Warehouse (12/31/97)
HR Planning & Forecasting

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

The workforce is aging with nearly 65% of the employees being 41 years of age or older.



1992 Total N = 19,404
1997 Total N = 16,322

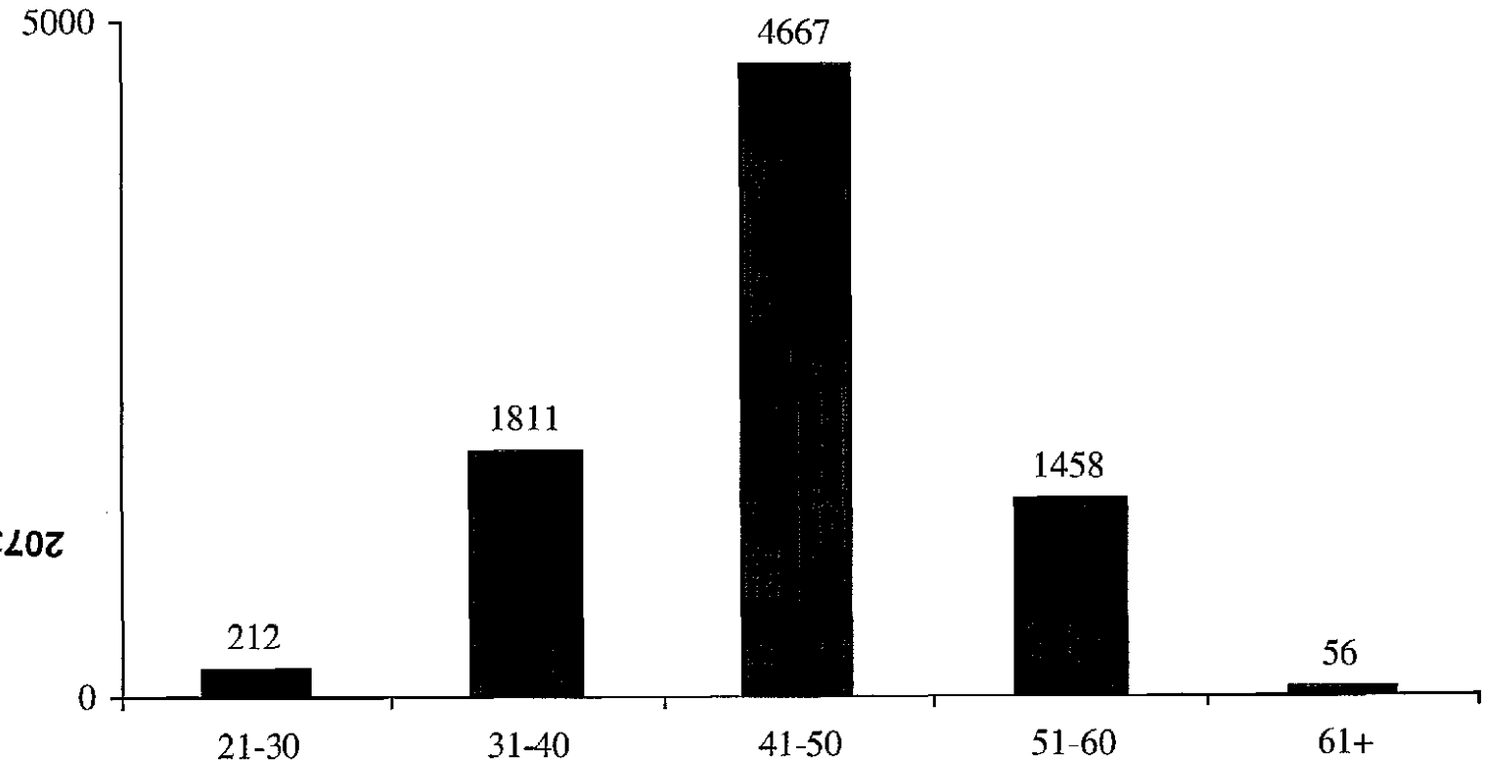
Source: Tesseract Warehouse by age bands (12/31/97)
HR Planning & Forecasting

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

In Manufacturing the aging situation is especially true of the hourly employees 75% of whom are 41 years of age or older.

1997 Demographics on Hourly Age Groups for Manufacturing

(Number of employees)



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Note: The total number of manufacturing hourly employees is 8,204 (excludes 48 hourly employees in R&D).

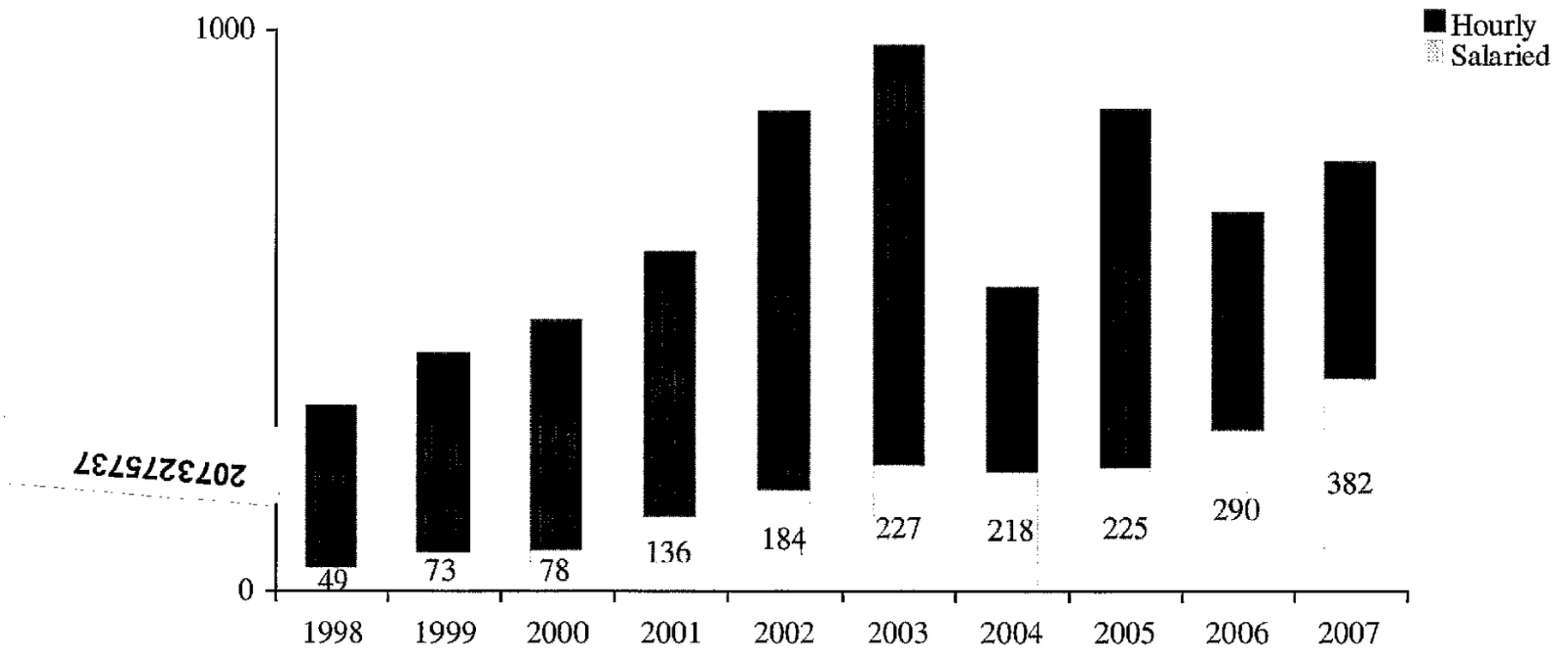
Source: Tesseract Warehouse 12/31/97
HR Planning & Forecasting

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Retirement opportunities are accelerating through the plan period especially amongst hourly employees.

Projected Workforce Eligible For Retirement

(Number of employees per year)



Source: FE-97-145 Hrly Retirement Projection charts (12/31/97)
FE-97-144 Salaried Retirement Projection charts (12/31/97)

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

The resignation rate amongst all exempt salaried employees has more than doubled since 1992.

Exempt Salaried
(# of Employees)

	1992			1997		
	Female	Male	Total	Female	Male	Total
Resignations	105	94	199	172	200	372
Total Exempt Population	2,062	4,999	7,061	2,100	4,557	6,557
% Resigned	5.1%	1.9%	2.8%	8.2%	4.4%	5.7%

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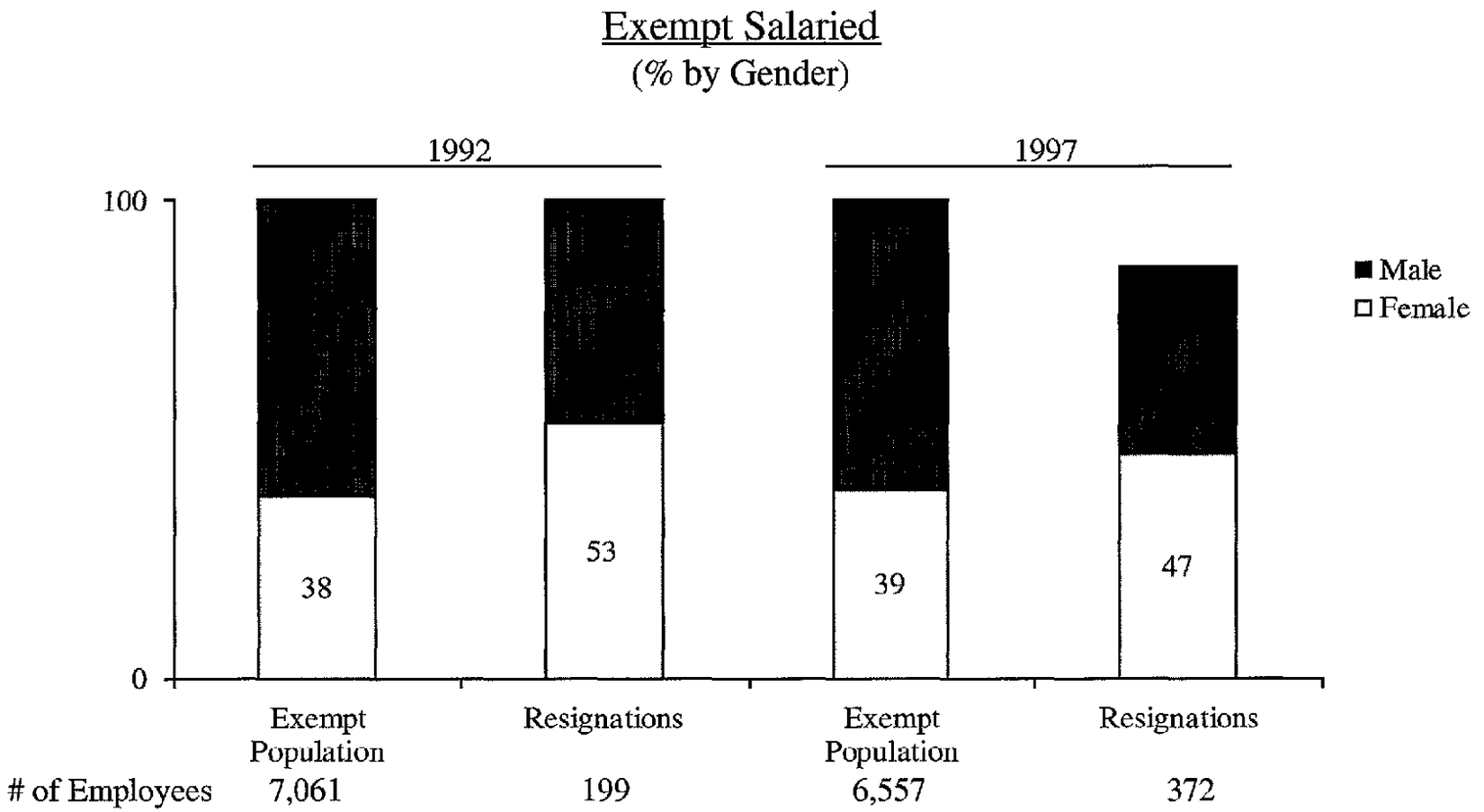
Source: HR Planning & Forecasting

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

The retention issue for exempt salaried females is worse than for males who leave at a slower rate.



2073275739

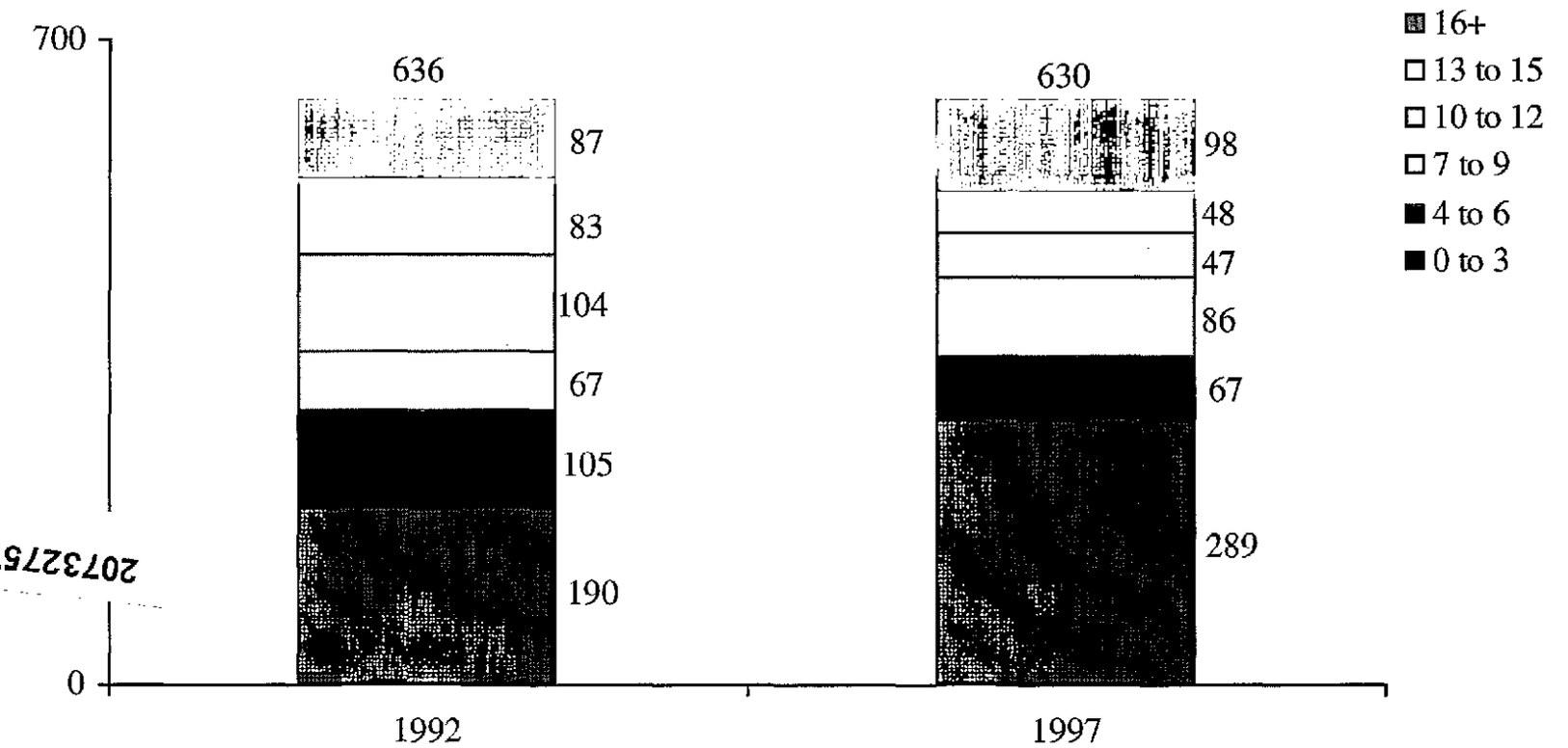
Source: HR Planning & Forecasting

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

3C. Strategic Principles	4. Capability

The retention rate for new hires has deteriorated and in 1997 46% of terminations occurred within 3 years of starting.

Salaried Terminations by Years of Service
(Number of employees)



Note: Above data reflects both resignations and discharges for both exempt and non-exempt salaried employees, including pending separations but excluding retirements.
Source: HR Planning & Forecasting
Tesseract Warehouse (12/31/97)

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Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

The exempt workforce is showing signs of grade inflation with the number of people in grades 12-17 increasing nearly 12% as the workforce population declines 7%.

Exempt Job Grade Analysis

(Number of employees)

Grade	1992	1997 [1]	Change #	Change %	
E11 & below	6167	5557	-610	-9.9	
E12	295	338	+62	+10.3	+11.7%
E13	308	327			
E14	117	148	+38	+15.1	
E15	73	87			
E16	40	40			
E17	21	14			
Banded Grades	40	46	+6	+15.0	
Total Exempt	7,061	6,557	-504	-7.1	

[1] Through 12/31/97
Source: HR Planning & Forecasting

2073275741

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

Bench strength is a critical issue.

End of Year 1997 Situation

PM-USA Succession Plan

- 17% of positions (E14 and up) have no "ready now" successors (50 out of 292[2]).
- 38% of incumbents have been in their job less than 1 year (110 out of 292[2]).

Key Positions identified by SLT[1]

- 24% of key positions have no "ready now" successors (16 out of 68[2]).
- 41% of incumbents in key positions have been in their jobs less than 1 year (28 out of 68[2]).

2073275742

[1] Senior Leadership Team
[2] Includes unfilled positions
Source: 1997 Succession Plan
HR Leadership Planning

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

The attrition rate for hires in Sales from the University Relations Program is three times greater than the regular salesforce attrition and is five times greater than regular salaried attrition.

Attrition Rates (1992 thru 1997)

(%)

University Relations Program	42[1]
Regular Active Salesforce	14
Regular Active Salaried	8
Total PM-USA	5

Note: Does not include retirements

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[1] Through 6/30/97

Source: 1992-1997 Workforce Summaries, HR Organization Learning & Development, Tesseract Database, HR Planning & Forecasting

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

3C. Strategic Principles	4. Capability

Continued investment in the company's Assessment and Leadership Development programs will be key in the selection and development of tomorrow's leaders.

Field Sales Learning Centers

1993-1997

	Total # Trained
DMs	88
DCMs	108
SAMs	141
UMs	578
TSMs	2,224
Total	3,189

Leadership Identification/ Effectiveness Programs

Grade Bandwidth	1991-Current Assessment	Number Part
(9-15)	CLE/CLI	375[a]

[a]26% on HIPO list

Leadership Development Programs

Grade Bandwidth	1989-Current Devmt. Progs.	Number Part
(10-15)	LDP/MMDP	217[b]
	MBA Assoc. Program Current Graduates	23[c]

[b]28% on HIPO list

[c]48% named successors/20 promoted

207327744

Source: HR Organization Learning & Development, HR Leadership Planning - Internal Tracking Systems

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003

We have a number of actions underway.

	1998 Actions Underway
Aging Workforce, especially hourly	• Rationalize future capacity requirements. • Provide ongoing training to create high-performance /better integrated work teams.
Low Retention Rates of new hires and females	• Study viability of flexible benefit programs. • Study expansion of variable pay. • Examining more flexible work/family arrangements (e.g. job sharing, tele-commuting, flexible work schedules, etc.).
Grade Inflation	• Clarify/improve communication of career pathways and opportunities. • Require more objective performance assessments by management. • Hold management accountable.
Succession Weakness	• Make more aggressive use of career pathing. • Develop special development programs as necessary.
Sales Recruitment & Retention	• Identify and rapidly move HIPOs thru early stages of career and move "blockers".

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Source: HR Executive office (1/28/98)

Source: https://www.industrydocuments.ucsf.edu/docs/pgpx0003